IN THE

Supreme Court of the United States

October Term, 1973
No. 73-1697

STANDARD PRESSED STEEL CO., a foreign corporation,
Appellant,

v.

DEPARTMENT OF REVENUE,
Appellee.

ON APPEAL FROM THE WASHINGTON STATE COURT OF APPEALS, DIVISION II

APPELLANT'S OPENING BRIEF

KENNETH L. CORNELL
and HAROLD S. FARDAL
KELLER, ROHRBACK, WALDO,
MOREN & HISCOCK
Attorneys for Appellant

Office and Post Office Address:
1220 IBM Building
Seattle, Wa. 98101
Telephone (206) 623-1900

CRAFTSMAN & MET PRESS SEATTLE, WASHINGTON

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OPINIONS BELOW

The Opinion of the Court of Appeals of the State of Washington, Division II, (A. 33) is reported at 10 Wn. App. 45, 516 P.2d 1043 (1973).

JURISDICTION

On December 3, 1973, the Court of Appeals of the State of Washington, Division II, filed its decision. (A. 33) Appellant thereafter, on December 20, 1973, filed its Petition for Rehearing, (A. 43) and that same court entered, on January 3, 1974, its Order Denying Appellant's Petition for

Rehearing. (A. 46) Appellant then addressed its Petition for Review (A. 47) to the Washington Supreme Court, the highest state court in which decision could be had, and that court, without hearing argument, entered its Order on February 20, 1974, denying appellant's petition for review. The decision of the Court of Appeals thereby became a final judgment on February 21, 1974. (A. 72) On March 14, 1974, Notice of Appeal (A. 74) to this court was filed with the Washington Court of Appeals, Division II, pursuant to Rule 11(3) of this court and 63 Stat. 104, 28 U.S.C. §2101(c). On May 13, 1974, the Jurisdictional Statement was filed and the case docketed in this court pursuant to Rule 13. Probable jurisdiction was noted on June 17, 1974, ... U.S. ..... The jurisdiction of this court rests on 62 Stat. 929, 28 U.S.C. §1257(2).

QUESTIONS PRESENTED[1]

1. Is a Washington tax on the privilege of engaging in the business of making sales at wholesale within said state repugnant to the due process clause of the United States Constitution when applied to gross receipts from sales of goods manufactured and sold wholly without the state by a foreign corporation to a customer located within the state, when the seller's sole-in-state activity consists of the activities of one resident engineer who makes himself aware of the customer's possible potential needs and passes this information to out-of-state offices, and who offers some engineering assistance to the customer in the use of the product, but who does not take or accept orders and who is not involved at all with sales negotiations, delivery dates or delivery problems, credit checks, or any other aspect of the sale transaction?

1. Repeated verbatim from Jurisdictional Statement.

Subsidiary to this question are the following:

a. Is such a tax an unwarranted extension of state power beyond its boundaries, so that traditional notions of fair play and substantial justice are offended?

b. Is the imposition of such a tax, a tax on de minimus activities and mere entry into the state?

2. Is the Washington tax on the privilege of engaging in the business of making sales at wholesale within said state repugnant to the commerce clause of the United States Constitution, when applied to the gross receipts from sales of goods manufactured and sold wholly without the state by a foreign corporation to a customer located within the state, when the seller's sole in-state activity consists of the activities of one resident engineer who makes himself aware of the customer's possible potential needs and passes this information on to out-of-state offices and who offers some engineering assistance to the customer in the use of the product, but who does not take or accept orders, and who is not involved at all with sales negotiations, delivery dates or problems, credit checks, or any other aspect of the sales transaction?

Subsidiary to this question are the following:

a. Does the commerce clause prohibit such a risk of multiple taxation where no sales activity of any kind occurs within the taxing state, where the necessary and material incidents of the sale occur outside of the taxing state?

b. Has the state afforded such a taxpayer sufficient protection and benefits to justify the exaction of the tax in return for said benefits?

STATUTES AND CONSTITUTIONAL PROVISIONS

The tax here involved is imposed by Title 82, Chapter 82.04 of the Revised Code of Washington (RCW). Pertinent portions of RCW Sections 82.04.040, 82.04.060, 82.04-070, 82.04.220, 82.04.270, and 82.04.500 are set forth in Appendix A hereto (infra pages A-1—A-3).

Article I, §8, cl. 3 of the Constitution of the United States (commerce clause) and the due process clause of the 14th Amendment to that Constitution are set forth in Appendix B hereto (infra page A-4).

STATEMENT OF THE CASE

This is an appeal by Standard Pressed Steel Co. from a final judgment of the Washington Court of Appeals sustaining assessments of the Washington business and occupation tax purportedly imposed on the privilege of "engaging within the state in the business of making sales at wholesale," RCW 82.04.270. The tax was levied on the unapportioned gross receipts of Standard Pressed Steel Co. resulting from its sales of aerospace fasteners (nuts and bolts generally) to Washington customers, sold wholly without the State of Washington and shipped to Washington customers, principally Boeing, by common carrier, f.o.b.

The hearings below were all conducted solely on oral argument with no live evidence being presented. Rather, the entire evidence in the case is in written form, consisting of a relatively short deposition of Robert Martinson (A. 75 *et seq.*). There are therefore no issues of credibility or demeanor, competency of witnesses, or the weighing or reconciling of conflicting testimony. This court is therefore in as good a position as the administrative bodies and

courts below to exercise its independent judgment on the evidence. This is particularly so where the dispute involves constitutional issues of law, namely, whether the imposition of the business and occupation tax on appellant is constitutionally justified. The courts and not administrative agencies possess the necessary expertise to decide questions of law such as those presented herein. Appellant therefore submits that this court, like the Washington Court of Appeals below, should exercise its independent judgment in its review of the record, and this court should not be deemed bound in any way by the findings and conclusions below.

Standard Pressed Steel Co. is a Delaware corporation with production facilities located in Jenkintown, Pennsylvania, and Santa Ana, California. (A. 77) A significant portion of appellant's business involves the manufacture and sale of highly machined fasteners for use in the aerospace industry, and, therefore, Standard Pressed Steel on occasion supplies fasteners to the Washington facilities of the Boeing Company. (A. 78, 90, 91)

The only employee of Standard Pressed Steel present within the State of Washington during the tax years in question was H. Robert Martinson, (A. 76, 80) an engineer, who at the time of his deposition in March of 1971, had been terminated by the company and who has not been replaced. (A. 76) Because Standard Pressed Steel's present operation in the State of Washington is different from that during the tax years in question in that there is presently no employee present within the state, the statement of the case will be in the past tense.

Martinson was paid a salary for his services, (A. 93) and performed his activities for appellant out of a portion

of one room in his home equipped with a desk, telephone and file cabinet. (A. 78) Appellant had no formal office in Washington (A. 78-80) and likewise did not maintain any warehouse, inventory, or outlet of any kind in the state. (A. 80, 93) It is undisputed that were it not for the activities of Martinson, appellant would not be subject to the tax.

Martinson's primary function was to attempt to inform himself, through contacts with Boeing Company qualification engineers, of possible needs of the Boeing Company for aerospace fasteners, and to pass this information on to appellant's out-of-state offices, describing the specifications required by the Boeing Company. (A. 76, 89, 94) There is nothing in the record to show that Martinson in anyway "created" a need for appellant's fasteners, or in any way promoted or "sold" appellant's product. Martinson's sole contact with Boeing was with Boeing qualification "project" engineers who could not purchase appellant's product even if they wanted to. (A. 77, 78)

As Martinson would receive information concerning possible needs for appellant's product as found in Boeing plans and drawings, Martinson would forward this information to appellant's out-of-state offices. (A. 76, 89, 94) After receiving this information from Martinson, Standard Pressed Steel personnel in Pennsylvania or California would make the decision as to whether or not appellant would even attempt to "qualify" as a supplier, either to Boeing or Boeing's sub-contractors. (A. 89) If the decision were to attempt to qualify, the company would manufacture sample qualification pieces and forward these directly to Boeing for qualification tests. (A. 85, 89) If the fasteners met the required specifications, Standard Pressed Steel was considered to be an "approved" source, and negotiations possibly leading to a sale would ensue between the Boeing Company and appellant's personnel located in either Pennsylvania or California. (A. 76, 77, 88, 89, 93, 94) Of course, competing aerospace fastener companies would also attempt to qualify as approved sources with the hope of ultimate sales of their fasteners.

All dealings in connection with possible sales and negotiations leading up to sales were carried on directly between the Boeing Company and appellant's sales personnel located in Pennsylvania or California. (A. 88, 89, 93, 94) Martinson was not in any way involved in these negotiations, either directly or indirectly, and was not consulted in any way, but rather was by-passed completely. Martinson had nothing to do with quoting, handling or relaying prices or delivery dates, handling or coordinating shipments, approving credit, and he did not solicit, accept or forward any orders for appellant's products. (A. 88, 89, 93, 94) All deliveries were made by appellant through a common carrier. If a problem developed relative to some aspect of the sale, Boeing did not call on Martinson but rather had to deal with appellant's personnel in either Pennsylvania or California. (A. 88, 89, 93, 94)

In addition to his forwarding information concerning Boeing's possible needs, which consumed the great majority of his time, Martinson also devoted some time (approximately 15%) to "troubleshooting". (A. 82-84, 94) If Boeing experienced any problems in the use of the product, Martinson would relay this information to appellant's engineering personnel in either California or

Pennsylvania, who would work to resolve the difficulties. The engineers would then forward this solution to Martinson, who would in turn present the proposed solution to Boeing engineers. (A. 82-89)

In addition to the above, approximately every six weeks or so Martinson would arrange hospitality meetings, lasting no more than three days, where appellant's engineers from out-of-state offices and Boeing engineers would meet and discuss engineering problems in the use of the product. (A. 81) Martinson would also on occasion inform appellant of the identity of various sub-contractors, purchasing specialists and control buyers of commodities, for which Standard Pressed Steel was an approved source. (A. 87-89) Martinson did not have any contact with such personnel, however. (A. 77, 78)

Standard Pressed Steel under protest has paid the tax claimed by the state to be due, and the parties have stipulated that the total amount of business and occupation taxes and interest subject to refund in the event petitioner is the prevailing party in this appeal is the sum of $33,-444.91.

SUMMARY OF ARGUMENT

First Question—Due Process.

It is well established that local taxation of a foreign corporation engaged in interstate commerce is justified only where the corporation is engaged in *substantial* income-producing activity in the taxing state. *Northwestern States Portland Cement Co. v. Minn.*, 358 U.S. 450; *Miller Bros. Co. v. Maryland*, 347 U.S. 340; *General Motors Corp. v. Washington*, 377 U.S. 436; and *Norton Co. v. Department of Revenue*, 340 U.S. 534. This is especially true in the case of a privilege tax on unapportioned gross receipts.

A review of the record clearly shows that appellant is not engaged in substantial income-producing activity in the taxing state. There is no precedent for imposing a tax on the privilege of conducting business within a state, measured by unapportioned gross receipts, where the in-state activities are so thin and inconsequential as those performed by appellant's engineer.

The court below nevertheless determined that appellant's instate activity was decisive in establishing and maintaining a Washington market. The conflict with *Norton Co. v. Department of Revenue*, 340 U.S. 534 (1950) is clear. In *Norton*, as to that class of sales held by this court to be exempt from the Illinois gross receipts tax, the Norton Co. was performing services within the state in connection with those sales through its corps of resident engineers who did not take or accept orders, but who did consult with customers as to their possible needs, and who offered engineering advice and assistance in the use of the product. Similarly, appellant's only in-state activity in connection with the sales in question is through its engineer who consults with the Boeing Company as to its possible need for the products, and who offers some engineering assistance and advice on the use of the products. On the authority of *Norton Co. v. Department of Revenue, supra*, such activities are not decisive factors in the sales and are not a sufficient nexus to support the imposition of a gross receipts tax on the privilege of making such sales.

In addition, in the present case, where the material ac-

tivities in connection with the sales occurred outside of the taxing state, the state is attempting to impose a tax on activities which occur beyond its borders, in violation of due process. *McLeod v. J. E. Dilworth*, 322 U.S. 327 (1944). The tax further goes far beyond the permissible bonds of due process, because its measure bears no fiscal relation to the protection, opportunities and benefits given by the state. *Wisconsin v. J. C. Penney Co.*, 311 U.S. 435. A tax which is not properly apportioned to business done within the jurisdiction denies due process. *Hans Rees' Sons, Inc. v. North Carolina*, 283 U.S. 123.

Second Question—Interstate Commerce.

The decision below held in part that the imposition of the tax was not repugnant to the commerce clause. Once again, the conflict with *Norton Co. v. Department of Revenue, supra*, is clear. In that case the court held that sales such as exist in the present case are so clearly interstate in character as to be exempt from the Illinois gross receipts tax. Like the Norton Co. on its exempt sales, appellant has not elected to localize itself in the Washington market, thereby gaining the advantages of a local business. Rather, the appellant, as seller, is seen by the customer as remote and inaccessible. Appellant likewise has not received benefits from the taxing state any more substantial than those received by taxpayers in such cases as *Miller Bros. v. Maryland*, 347 U.S. 340; *Norton Co. v. Department of Revenue*, 340 U.S. 534 (on exempt sales); *McLeod v. J. E. Dilworth Co.*, 322 U.S. 327; *Gwin, White & Prince, Inc. v. Henneford*, 305 U.S. 434; *Robbins v. Shelby County Taxing District*, 120 U.S. 489; *Nippert v. City of Richmond*, 327 U.S. 416; *Freeman v. Hewit*, 329 U.S. 249; and

National Bellas Hesse v. Department of Revenue, 386 U.S. 753, and in all of these cases the imposition of the tax was struck down.

In this case, the material incidents of the transaction occur in either Pennsylvania or California, and the taxing situs of the privilege of conducting the transaction is in Pennsylvania or California. While these states do not have such a privilege tax at the present time, the risk of repeated exaction of the tax is clear. To rule that the question of multiple taxation is not properly before this court would subject the appellant to the vagaries and whims of various state legislatures. Appellant submits it is this very type of multiple exposure which the commerce clause was designed to prevent. *Freeman v. Hewit*, 329 U.S. 249.

If the decision of the court of Appeals below is upheld, it will be to the detriment of the national market, and it will encourage interstate businesses either to become for all intents and purposes domestic businesses, or to sever their already thin contacts with the taxing state so as to avoid taxation entirely, which places interstate commerce at a further competitive disadvantage.

ARGUMENT

First Question—Due Process.

An examination of the principles of the commerce clause and the due process clause of the Fourteenth Amendment as applied to the ability of a state to tax foreign corporations engaged in activities within the state, reveals an interplay and overlap of the two concepts in application and analysis. As a result, much of the argument herein under the due process heading applies to the argument presented

under the commerce clause heading and vice versa. For this reason, portions of the argument presented may be repeated in measure under both headings.

The test of the power of a state to impose a tax on a concern operating in interestate commerce is to determine whether the tax is so closely related to the local activities of the concern as to form some definite link, some minimum connection, between the state and the person, property or transaction sought to be taxed. *Miller Bros. Co. v. Maryland,* 347 U.S. 340. In applying this test, the court has directed its inquiry to the amount and effect of the local activities and has required that the local activities be substantial in relation to the incidence of the tax and in some way promote sales, *e.g., Miller Bros. Co. v. Maryland,* 347 U.S. 340, where the court struck down the imposition of a sales tax even though there were deliveries of purchases into the taxing state and mailing of notices of special sales to residents of the taxing state; *American Oil Co. v. Neill,* 380 U.S. 451, where it was held that it was constitutionally impermissible to suppose that the interstate activities of the appellant contributed in any way to the transaction in question where every material phase of the sales transaction occurred outside of the state; *McLeod v. J. E. Dilworth Co.* 322 U.S. 327 (1944), where the local sales tax was held invalid as applied to goods shipped f.o.b. into state by an out-of-state manufacturer, and where sales orders were solicited by "drummers", subject to acceptance at the head office; *Norton Co. v. Department of Revenue,* 340 U.S. 534, where the court held a gross receipts privilege tax invalid where the only interstate activity associated with those sales was conducted by a group of engineers who consulted with customers as to their needs and who

offered technical assistance and advice in the use of the product; *General Motors Corp. v. Washington, supra,* where the court expressly found substantial and extensive promotional activity and an in-state bundle of corporate activity enmeshed in an admittedly local maze of taxable business and further observed that in-state activity of a de minimus nature, constituting mere entry into the state, is not a sufficient nexus; and *Northwestern States Portland Cement Co. v. Minnesota,* 358 U.S. 450 (1959), where the court stated that where a taxpayer is not a domiciliary of a state, that state can tax the net income of a foreign business only when the taxpayer engages in substantial local activities. The Washington Supreme Court in *General Motors v. Washington,* 60 Wn.2d 862, 376 P.2d 843, *aff'd* 377 U.S. 436, stated that taxation of interstate concerns which performed de minimus activities within the state would be both unreasonable and unjust.

As is the case with any application of due process, the court's interpretation of due process varies with the nature of the particular tax in question. *Eli Lily & Co. v. Sav-on Drugs,* 366 U.S. 276. In *Norton* the court observed that nexus is more easily established in a sale or use tax context because of the impact of the taxes on the local buyer-user, and cases involving those taxes are not controlling where an unapportioned tax falls on the vendor, such as exists in the case at bar. As to the amount and effect of contacts necessary to establish a constitutional nexus in the situation of a privilege tax measured by gross receipts, the two cases most clearly in point are *Norton Co. v. Department of Revenue,* 340 U.S. 534, and *General Motors Corp. v. Washington,* 377 U.S. 436.

That appellant's in-state activity is not sufficient to establish a constitutional nexus with the taxing power of the state was established in *Norton*, which is a case remarkably similar to the case at bar, and is controlling authority in support of appellant.[2] In *Norton* the court held that where a non-resident manufacturer maintains an in-state office staffed with consulting liaison engineers who do not solicit or take orders, the activities are not sufficient to justify on due process grounds the imposition of the Illinois occupation tax measured by gross sales.

The facts in *Norton* were that the Norton Company was a producer of industrial grinding wheels and abrasive materials used in manufacturing. The Norton Company maintained a large sales office and warehouse in Chicago and made over the counter retail sales to customers, which the Norton Company admitted were subject to the state business and occupation tax. The Norton Company did, however, challenge the imposition of the occupation tax measured by gross sales to Illinois customers as to four different classes of sales, alleging in part that the in-state activities associated with those sales were not sufficient to justify the tax. The taxes on three of the four classes of sales in question were upheld as constitutional. As to those direct sales held to be exempt and nontaxable, however, the local activities were held to be de minimus, constituting mere entry at best, and not decisive factors in establishing and maintaining the Illinois market. The local activities involved with these direct sales were performed by

2. See *B. F. Goodrich Co. v. State*, 38 Wn.2d 663, 231 P.2d 325 (1951), where the Washington Supreme Court, in considering similar challenges to the tax question, expressly stated that *Norton* was controlling authority, and *Field Enterprises, Inc. v. Washington*, 47 Wn.2d 852, aff'd 353 U.S. 806, where the court deemed *Norton* to be controlling authority.

Norton's corp of engineers, who did not take or solicit orders, but who did consult with customers as to their needs,[3] and who offered technical engineering assistance and advice in the use of the product,[4] all of which activity was held to be an insufficient local contact, such that taxation would be unjust and unfair.

As in the case of the Norton Company engineers, in the case at bar the only in-state activity involved is that of appellant's one engineer who did not take or solicit orders and who offered a measure of technical engineering assistance and advice in the "trouble-shooting" process, and did not consult with Boeing as to their future needs, but rather passed on information of which he became aware concerning possible future needs of Boeing. Based on the facts of the case at bar, it cannot be said that appellant performed local services any more essential to the ultimate sale or performed services any more significant than did the Norton engineers on the exempt sales. Nevertheless, the Washington Court of Appeals determined that Martinson's activity was a "sufficient peculiarly localized" distinctly taxable incident within the State of Washington, in that his actvitiy enabled Standard Pressed Steel to:

> "(1) become aware of which of its products the Boeing Company might be able to use; (2) secure the testing of sample products to qualify the products for sale to the Boeing Company;(3) obtain the engineering designs for such products; (4) resolve problems in the use of the products after receipt and use by the Boeing Company; (5) obtain and retain goodwill and working rapport with Boeing personnel; and (6) secure and update lists of Boeing purchasing specialists

3. *Norton Co. v. Department of Revenue*, 405 Ill. 314, 90 N.E.2d 737 (1950).

4. *Norton Co. v. Department of Revenue*, 340 U.S. 537.

> or control buyers, and the commodities for which they are responsible, for the use of the personnel at the plaintiff's home office." (A. 37)

The conclusion that Martinson's activity was sufficient local taxable incident is clearly in conflict with *Norton*. A review of the record show that Martinson's primary duties were the same as those of the Norton engineers. Both Martinson and the Norton engineers were concerned with the prospective needs of customers. Both Martinson and the Norton engineers supplied a measure of engineering and technical advice in the use of their respective products. Certainly, the Norton engineers were concerned with obtaining and retaining good will and rapport with their company's customers, and their efforts were performed for the purpose of aiding the direct sales held to be non-taxable.

The circumstances of the case at bar present an even clearer case for exemption from taxation than that faced by the court in *Norton*. Appellant is not conducting a local outlet of any kind within the state requiring appellant to show the transactions as disassociated from the local business. In addition, the activities of the Norton engineers in consulting with customers as to needs constitutes activity of a more substantial nature than the activity of appellant's engineers in merely becoming aware of Boeing's possible needs. Implicit in the consultation of Norton engineers with customers is an element of persuasion, inducement or salesmanship of the product, which factors are missing in Martinson's activity. As stated previously, Martinson merely reviewed design drawings and specifications to become aware of Boeing's "self-induced" or "self-perceived" possible future needs. Martinson did not in any

way create the need or attempt to influence Boeing to use appellant's products. Boeing's need for fasteners was rather created independent of Martinson or Standard Press Steel. Martinson was placed in Washington therefore primarily not to "benefit" the customer or the Boeing Company by presenting or promoting appellant's products, but rather to give appellant as much advance lead time as possible in the qualification process. It is true that Martinson did spend a small percentage of his time in the trouble-shooting process, but as observed in *Norton*, the Norton engineers in addition to consultation as to needs, likewise offered technical engineering assistance and advice in the use of the product.

Clearly on the authority of *Norton*, the State of Washington cannot constitutionally subject appellant to the state business and occupation tax. If an out-of-state company, with an extensive local sales office cannot be taxed on its direct orders to the manufacturer, where the company maintains a corps of liason engineers to consult with the customers who order direct, clearly under the facts of the case at bar, where there is no local sales activity of any kind, no local outlet, all sales being of the direct order type, appellant cannot constitutionally be subject to the business and occupation tax.

Appellee has consistently throughout the course of this case taken the position that the Norton Company engineers did not perform activities associated with tax exempt sales. A careful reading of the *Norton* opinion shows this contention to be without merit. As noted previously the Norton engineers consulted with prospective customers as to their needs and offered technical engineering assist-

ance and advice in the use of the Norton products. Picture these engineers in their office, available to consult with a customer. A customer, or prospective customer, contacts one of these engineers with a problem or a question concerning a Norton product. Contrary to appellee's interpretation of *Norton*, it is certainly not reasonable to assume that prior to consulting with the customer the engineer would inquire as to whether the customer was placing his order direct to Massachusetts and receiving shipment directly back, in which case the engineer would decline to render services, or whether the customer expected the help of the Chicago outlet on some aspect of the sale, and, if so, to what extent. And what would the engineer do if the customer had not yet decided how the order would be placed? And further, such an inquiry would only be relevant after the *Norton* decision in any event, unless appellee would have us assume further that the Norton engineers were able to predict the result in *Norton*. In addition there is nothing in the *Norton* opinion which states or implies that these engineers were not offering engineering assistance to customers involved in direct sales. On the contrary, the *Norton* opinion describes the engineers as providing engineering assistance without limitation. If the Norton engineers did not provide engineering assistance to a certain class of customers, such a critical fact would certainly have been mentioned in the opinion.

In spite of the clear support the *Norton* decision provides for appellant's position in this case, the Washington Court of Appeals apparently concluded that *Norton* did not compel a judgment in favor of appellant and distinguished *Norton* on the basis that implicit in the *Norton* decision was the conclusion that the activities of the local Chicago

office, including the activities of the engineers, were not decisive factors in holding or establishing the market reflected by the direct interstate sales, while Martinson's activity in the State of Washington was instrumental in establishing and maintaining the Boeing Company as a market. What the Court of Appeals overlooked in its opinion is that Martinson's activities are substantially the same activities as were performed by the Norton engineers. If the services of the Norton engineers were held to be not decisive factors in holding the market on direct sales, it naturally follows that the activities of Martinson must likewise be held to be insufficient and non-decisive factors in establishing and maintaining the Boeing Company as a market.

The incorrect legal result reached by the Washington Court of Appeals results in part from a misreading of the *Norton* opinion, stemming from the decision of the Washington Supreme Court in *B. F. Goodrich Co. v. State*, 38 Wn.2d 663, 231 P.2d 325 (1951). As stated by the Court of Appeals, (A. 40):

> "The *Norton* decision was construed by our State Supreme Court as follows:
>
> > 'We only interpret the *Norton Co.* case as holding that such a tax may not be levied upon the proceeds from sales with which the local outlet had nothing to do'.
>
> "*B. F. Goodrich Co. v. State*, 38 Wn.2d 663, 675, 231 P.2d 325 (1951)."

In *Goodrich*, the Washington Supreme Court obviously disagreed with the result in *Norton* on the non-taxable sales, and reluctantly applied the case as sparingly as possible. Instead of reading the opinion as resting on the

proposition that the conducting of an intrastate business was the taxable event and that the taxpayer's interstate business was taxable only to the extent that it could not be separated from the local business, the court declared that *Norton* permitted a state to impose its gross income tax on all interstate commerce except where there was no in-state activity at all associated with sales, and held taxable every transaction that had any contact, however tenuous, with an in-state office. The *Goodrich* opinion set the tone for all subsequent judicial rulings in the State of Washington on such matters, and clearly influenced the Court of Appeals in its evaluation of the activities of Standard Pressed Steel in the State of Washington. Such on interpretation of the law, however, finds no support in the decisions of this court.

The later case of *General Motors Corp. v. Washington*, 377 U.S. 436 does not weaken the holding of *Norton*, but rather reaffirms the principles of *Norton*, and supports appellant's position herein.

In *General Motors*, the court considered the activities of one of the largest corporations in the world, with the corporation conducting a maze of in-state activities which admittedly were subject to the taxing power of the state. As to the challenged classes of sales, the activities of the corporation in the state covered several pages of the court's opinion, and the court concluded:

> "That the tax is levied on the incidence of a substantial local business in Washington." (377 U.S. at p. 439).

As to the challenged classes of sales, the facts showed that during the tax period involved, the Chevrolet, Oldsmobile, and Pontiac Divisions had an average of twenty em-

ployees resident or principally employed in Washington, with General Motors Parts Division employing about twenty more. These employees were in addition to other employees working out of the Portland Zone Office, who would regularly and systematically visit dealers to secure and maintain a quality dealer organization, with the aim of achieving better sales results. These employees would advise dealers on divisional sales policies and promotional and training plans to increase sales. Projections of orders of estimated needs were prepared by General Motors personnel, which projections were purchase orders for all practical purposes. General Motors' service representatives advised dealers on methods of increasing service efficiency. The zone used car managers assisted Washington dealers in the disposition of used cars through appropriate display and reconditioning. The Parts Division had a warehouse and inventory in Seattle. Based on these actions and others not mentioned herein, the court correctly concluded that the corporation was conducting extensive and substantial promotional and service efforts. The activities of General Motors in Washington are in sharp contrast to appellant's one engineer whose basic activities did not in any way promote sales or offer customer benefits, and whose activity was similar to the activity of the Norton engineers. There is no possible justification for equating the amount and effect of Martinson's activities with the bundle of corporate activities and maze of local connections of General Motors in the State of Washington. It is clear that General Motors had established and was operating a local business and was not seen by customers as remote and inaccessible. As stated in *American Oil Co. v. Neill*, 380 U.S. 451, where a corporation pursuant to permission given, enters a state and estab-

lishes a local outlet, the imposition of a tax will not violate due process. It cannot be said, however, that appellant had established a local outlet within the meaning of *Norton* and *General Motors*, through which appellant has gained the advantages of a local business. Appellant rather has approached the market in a manner in which the Washington customer views appellant as remote and distant with the customer having to deal with appellant's personnel located in distant states.

The activities of appellant which are sought to be taxed are the Washington activities involved in the wholesale sales to Boeing. The record clearly shows however that all necessary incidents to the sales were performed by appellant directly from its offices located in either Pennsylvania or California. The court has never sustained a tax on the privilege of conducting business within a state where the in-state activities are so thin and inconsequential as those performed by appellant's engineer. When compared with the incidence of the sales which occurred outside the state, the activity on which the tax is based is de minimus indeed. To uphold the tax assessment on appellant is to impose a tax on activities which occur beyond the borders of the state. This is a violation of due process. *McLeod v. J. E. Dilworth Co.*, 322 U.S. 327. It is clearly unfair and unjust to require appellant, who has elected to carry on its business in interstate commerce with all of its essential and material activities in connection with the Washington sales taking place outside of the boundaries of the state with only incidental and de minimus activity within the State of Washington, to pay the same tax that would be payable if all of its activity in connection with the Boeing sales occurred in Washington.

It is also a violation of due process for a state to impose a tax, the measure of which does not bear a reasonable fiscal relationship to the protection and benefits conferred by the state on the intrastate activities which give rise to the tax. *Wisconsin v. J. C. Penney Co.*, 311 U.S. 435. In other words, this tax violates due process as it is not properly apportioned to the business done in the taxing jurisdiction. *Hans Rees' Sons, Inc. v. North Carolina*, 283 U.S. 123. In that case the North Carolina statute imposed a tax measured by a portion of net income, but the apportionment formula attributed 80% of the taxpayer's income to North Carolina, whereas it appeared that in fact no more than 17% actually arose there. The result was unconstitutional. The result here is much more aggravated. The tax applies to 100% of receipts, and while appellant has no precise measure of the amount attributable to in-state activities, it should be obvious that it cannot be other than de minimus.

In the present case the Washington Court of Appeals has erred, not only in finding a "taxable incident" but in holding that there being such an incident, the measure of the tax based upon that incident is constitutional. In *Gwin, White & Prince, Inc. v. Henneford*, 305 U.S. 434, involving this very tax, this court in holding to the contrary, stated at page 438 that:

> "While appellant is engaged in business within the state, and the state courts have sustained the taxes laid on its activities there, the interstate commerce service which it renders and for which the taxed compensation is paid is not wholly performed within the state. A substantial part of it is outside the state where sales are negotiated and written contracts of sale are executed, and where deliveries and collec-

> tions are made. Both the compensation and the tax laid upon it are measured by the amount of the commerce—the number of boxes of fruit transported from Washington to purchasers elsewhere; so that the tax, though nominally imposed upon appellant's activities in Washington, by the very method of its measurement reaches the entire interstate commerce service rendered both within and without the state and burdens the commerce in direct proportion to its volume."

It might be argued however, that certainly Standard Pressed Steel has received benefits from the state for which the state can exact a fair return. While the tax in question does not allow for a fair return but rather is unapportioned, it should be clear that the State of Washington in any event has not given anything to Standard Pressed Steel for which it can ask return, any more than the various states involved provided benefits and protection to the taxpayer in such cases as *Miller Bros. v. Maryland*, 374 U.S. 340; *Norton Co. v. Department of Revenue*, 340 U.S. 534 (on the exempt sales); *McLeod v. J. E. Dilworth Co.*, 322 U.S. 327; *Gwin, White & Prince, Inc. v. Henneford*, 305 U.S. 434; *Robbins v. Shelby County Taxing District*, 120 U.S. 489; *Nippert v. City of Richmond*, 327 U.S. 416; *Freeman v. Hewit*, 329 U.S. 249; and *National Bellas Hesse v. Department of Revenue*, 386 U.S. 753, and in all of these cases the imposition of the state tax was struck down.

Second Question—Commerce Clause

While a concern operating in interstate commerce might have sufficient contacts with the state to justify the imposition of a tax on a due process basis, the strictures of the Constitution do not end there, as it is settled that a state may not tax the privilege of engaging in interstate commerce, *Spector Motor Service, Inc. v. O'Conner*, 340 U.S.

602. In this regard it is settled for a state to levy a tax upon a business operating in interstate commerce, the circumstances must be such that the taxpayer has elected to operate and compete as a local business with the competitive advantage of a local business. *Miller Bros. v. Maryland*, 374 U.S. 340. And in *Norton Co. v. Department of Revenue*, 340 U.S. 534 the court declared at page 534:

> "Although the concern does not, by engaging in business within the state, lose its right to do interstate business with tax immunity, *Cooney v. Mountain States Telegraph Co.*, 294 U.S. 384, it cannot channel business through a local outlet to gain the advantage of a local business and also hold the immunities of an interstate business."

That the imposition of the tax in the present case is in violation of the commerce clause as being a tax on the privilege of conducting a purely interstate business was established in *Norton Co. v. Department of Revenue*, 340 U.S. 534, where it was held that direct sales were so clearly interstate in character as to be non-taxable as the only in-state activity was that of a corps of resident engineers who consulted to customers as to needs and who offered engineering assistance and advice. Similarly, in the case at bar where appellant's activities were the same or sufficiently similar to the activities of the Norton engineers, appellant's sales are clearly interstate in character, such that the imposition of the Washington business and occupation tax constitutes a tax on the privilege of engaging in interstate commerce.

The basis of the court's holding in *Norton* was that the amount and effect of the activities of the Norton Co. on the three taxable classes of sales were such that the company had elected to localize itself in the Illinois market

with the advantages of an interstate business. In such a case where a business allegedly operating in interstate commerce has elected to compete on much the same basis as a local intrastate business with substantial local connections and with the competitive advantages which go along with a local business, it is not within the contemplation of the commerce clause, and it would be unreasonable, to allow such a business to hold the immunity of an interstate business. On the direct exempt sales however, where the only activity was that of the engineers, the business was not competing on the level of a local business and did not have the advantages of a local business. From a competitive point of view, such an operation has competitive disadvantages as the trade is likely to view the seller as remote and inaccessible. The seller cannot supply items from a local outlet, communication is more difficult, freight and shipping are more difficult, problems in general are more difficult to solve, and freight costs are generally greater for the customer. This is exactly the type of operation which the commerce clause protects by providing an immunity from the taxing power of the state. As observed in *Norton,* 340 U.S. 534, 536:

> "Where a corporation chooses to stay at home in all respects except to send abroad advertising or drummers to solicit orders which are sent directly to the home office for acceptance, filling and delivery back to the buyer, it is obvious that the state of the buyer has no local grip on the seller. Unless some local incident occurs sufficient to bring the transaction within its taxing power, the vendor is not taxable. . . .
>
> "This corporation could have approached the Illinois market through solicitors only and it would have been entitled to the immunity of interstate commerce as set out in the *Dilworth* case. From a competitive point of

> view, that system has disadvantages. The trade may view the seller as remote and inaccessible. . . . Petitioner elected to localize itself in the Illiniois market with the advantages of a retail outlet in the state, to keep close to the trade, to supply locally many items and take orders for others and to reduce freight costs to local consumers. Although the concern does not, by engaging in business within the state, lose its right to do interstate business with tax immunity, *Cooney v. Mountain States Telegraph Co.,* 294 U.S. 384, it cannot channel business through a local outlet to gain the advantage of a local business and also hold the immunities of an interstate business."

Examples of other decisions of this court in accord with *Norton* include *Miller Bros. v. Maryland,* 347 U.S. 340, where the court struck down the imposition of a sales tax on the basis that the taxpayer had not exploited or invaded the consumer market in Maryland; *McGoldrick v. Berwind-White Coal Mining Co.,* 309 U.S. 33, where the court stated that the commerce clause does not forbid taxation of a local business which is separate and distinct from interstate commerce; and *Freeman v. Hewit,* 329 U.S. 249.

In the case at bar it is clear that in no sense of the term has appellant elected to localize itself in the Washington market, thereby gaining the advantages of a local business. Rather, like the solicitor cases referred to in *Norton,* the appellant as seller is seen as remote and inaccessible. The Boeing Company and other Washington customers in dealing with appellant dealt directly with appellant's offices located in distant parts of the country, in different time zones, with communication and freight problems which would not exist if appellant were a local business. Based on *Norton,* it cannot be said that appellant by virtue of the activity of its engineer had elected to localize itself any

more than the Norton Co. had on their direct sales held to be exempt. The State of Washington, therefore, cannot tax appellant on the same basis as a local business.

It might be argued that in spite of the above, nevertheless appellant has received some benefits and services from the state for which the state can exact a fair return. Appellant however has received no more benefits from the state than have taxpayers in those cases where the imposition of a tax was declared unconstitutional.[5]

If imposition of the tax on appellant is upheld, it will be to the detriment of the national market. Appellant has chosen to deal with Washington customers not as a local business, but as a concern with all the inherent competitive disadvantages of interstate business. The Washington tax because it is unapportioned nevertheless taxes appellant as if appellant were a local concern. If such a tax is upheld, because of the basic unfairness of being taxed as a local business while not operating as such, appellant and other interstate concerns will be encouraged to either become more local in nature and to establish true local outlets, which is exactly the sort of forced provincialism the commerce clause was designed to protect against, or interstate concerns will sever their already thin contacts with the state, which would place interstate commerce at an unnecessarily further competitive disadvantage. In either case, domestic intrastate business would be further encouraged to deal with other "domestic" businesses to the detriment of the national market.

As stated previously, it is clear from the record that all of the essential and material incidents in connection with

5. See *supra*, page 24.

the Boeing sales occurred outside of the State of Washington. In such a case not only is there substantial risk of multiple tax burdens, it would appear that Pennsylvania and California may be the only states who can in any way tax appellant's sales of Boeing, and therefore the sales to Boeing are exempt from the Washington business and occupation tax. *Gwin, White & Prince, Inc. v. Henneford,* 305 U.S. 434. The Washington Court of Appeals dismissed this contention on the basis that appellant has not affirmatively shown that its activities are being taxed elsewhere on the basis of the majority opinion in *General Motors Corp. v. Washington,* 377 U.S. 436. Appellant submits however that the sounder analysis of multiple burdens is that advanced by Justice Goldberg in his dissent in *General Motors,* where with respect to the view that the application of the commerce clause depends upon the existence of actual multiple taxation, the following quote from *Freeman v. Hewit,* 329 U.S. 249, at 256 was presented:

> It is suggested . . . that the validity of a gross sales tax should depend upon whether another State has also sought to impose is burden on the transaction. If another State has taxed the same interstate transaction, the burdensome consequences to interstate trade are undeniable. But that, for the time being, only one State is taxed is irrelevant to the kind of freedom of trade which the commerce clause generated. The immunities implicit in the commerce clause and the potential taxing power of a state can hardly be made to depend in the world of practical affairs, on the shifting incidents of the various tax laws of the various states at a particular moment. Courts are not possessed of instruments of determination so delicate as to enable them to weigh the various factors in a complicated economic setting which, as to an isolated application of a State tax, might mitigate the obvious burdens generally created by a direct tax on commerce."

The requirement that the taxpayer show actual as opposed to an exposure to the risk of multiple burdens puts a very heavy and almost impossible burden on a taxpayer. In requiring actual multiple burdens, the result is that the first state to tax preempts other states from levying a similar tax if that tax would create a multiple burden, even though it would have been fairer in the first instance for the second state to have imposed the tax. In requiring actual multiple burdens to be affirmatively shown, a situation can arise where a tax valid in one state is invalid in another, even though the same activity occurs within each state.

The state may contend that there can be no risk of multiple burdens in the present case since only the activities within the State of Washington are those being taxed with gross receipts to Washington customers being the measure. It is submitted however that since the essential wholesaling activities resulting in sales to Boeing take place in either Pennsylvania or California, those states could also impose a tax on the activities occurring in those states for the privilege of conducting wholesaling activities with the measure of the tax being the same gross receipts of sales to Washington customers. The reality of this risk is especially apparent where we have an unapportioned tax. If California and/or Pennsylvania were to impose such a tax, appellant would certainly be subject to actual multiple taxation, not borne by local commerce, and as a result would be at a competitive disadvantage with local commerce.

CONCLUSION

Appellee department of Revenue has assessed against appellant Standard Pressed Steel a "business and occupation tax" measured by unapportioned gross receipts of all sales by appellant to Washington customers, purportedly "for the act or privilege of", RCW 82.04.220, "engaging within this state in the business of making sales at wholesale", RCW 82.04.270. The taxed receipts were from the manufacture and sale of goods wholly without this state, with the in-state activity being merely that of one engineer who was not involved in any way in sales promotion or in the sales transaction.

The assessments are invalid because of lack of substantial income producing activity in the state, which is necessary to form some definite link, some minimum connection with the taxing power of the state. *Miller Bros. Co. v. Maryland,* 347 U.S. 340. Rather, appellant's in-state activity in relation to the incidence of the tax is of a de minimus nature, constituting mere entry into the state, and taxation of such activity is both unreasonable and unjust. *Norton Co. v. Department of Revenue,* 340 U.S. 534; *General Motors Corp. v. Washington,* 377 U.S. 436. If the Norton Co., with its extensive local sales office cannot be taxed on its direct order sales with in-state activity connected with such sales conducted by its corps of engineers, clearly in the case at bar, where there is no local sales activity of any kind, the assessments by appellee violate due process.

The assessments are invalid as a tax on activities which appear to be outside the borders of the state. As shown by the record, all of the necessary and material incidents to

the Washington sales were conducted in either Pennsylvania or California. To uphold the tax assessment on appellant is to impose a tax on activity over which the state has no jurisdiction. This is a violation of due process. *McLeod v. Dilworth*, 322 U.S. 327.

The tax is invalid as it does not bear a reasonable fiscal relationship to the insignificant benefits conferred by the state. *Wisconsin v. J. C. Penney Co.*, 311 U.S. 435. In other words, the tax involved violates due process as it is not properly apportioned to the activities conducted in the taxing jurisdiction. *Hans Rees Sons, Inc. v. North Carolina*, 283 U.S. 123.

The tax is invalid as a tax on the privilege of conducting business solely in interstate commerce. *Norton Co. v. Department of Revenue*, 340 U.S. 534. Appellant in no sense of the term has elected to operate and compete as a local business with the competitive advantages inherent thereto. Rather, appellant by operating in interstate commerce is viewed by customers as remote and inaccessible, and appellant is therefore operating at a competitive disadvantage with intrastate business. The assessments are therefore repugnant to the commerce clause. *Norton Co. v. Department of Revenue*, 340 U.S. 534; *Miller Bros. Co. v. Maryland*, 347 U.S. 340. Certainly, to impose a tax on appellant the same as if all of its activity in relation to Washington sales occurred locally, is unreasonable, unjust, and repugnant to both the commerce clause and the due process clause.

The tax assessments are invalid because they expose appellant to the risk of repeated and multiple tax burdens. *Freeman v. Hewit*, 329 U.S. 249. Under the facts in the case at bar, where all of the material incidents in connection

with the sales occur outside of the state, it would appear that Pennsylvania and California are the only states which in any way can tax appellant's sales to Boeing. If the court were to defer on the basis that there is no showing of actual multiple taxation, the immunities implicit in the commerce clause would be made to depend on the vagaries and shifting incidents of the various state legislatures.

The opinion below rests on the erroneous rule of law that any activity within the state, regardless of the amount and effect of such activities, is a sufficient local incident to justify the assessments, and since the tax on the gross receipts is only a measure of the tax on such in-state activities, there can be no interference with interstate commerce. The result of the decision below, if left to stand, is that a taxpayer who has not elected to compete on a local basis and who does not have the advantages of local business, nevertheless has lost its immunity from taxation, and the state will be exacting tax without providing sufficient benefits in return. This would introduce serious uncertainty in interstate business. Firms once considered exempt would be considered fair game and would be in jeopardy. Such a weakening of the constitutional protections would result in interstate business receiving only negligible protection if at all. If the decision below is left to stand, *Norton Co. v. Department of Revenue*, 340 U.S. 534, will of necessity, be overruled. Activities previously held by this court to be insufficient to justify a business and occupation privilege tax will now be sufficient. This decision below will extend the taxing power of a state to the detriment of the national market. In every prior instance where the taxing power of a state, including Washington, has been upheld on appeal, far more significant in-state activity in connection with its

transactions has been present than exists here, especially where the tax was a privilege tax measured by unapportioned gross receipts. There is no precedent for upholding the decision below where the activities of appellant within the state are so thin and insubstantial.

The judgment of the Washington Court of Appeals should be reversed and remanded with directions to refund to appellant the sum of $33,444.91.

Respectfully submitted,

KENNETH L. CORNELL
and HAROLD S. FARDAL
KELLER, ROHRBACK, WALDO,
MOREN & HISCOCK
Attorneys for Appellant

APPENDIX A

STATUTES

Chapter 82.04 of the Revised Code of Washington

82.04.040 *"Sale," "casual or isolated sale."* "Sale" means any transfer of the ownership of, title to, or possession of property for a valuable consideration and includes any activity classified as a "sale at retail" or "retail sale" under RCW 82.04.050. It includes renting or leasing, conditional sale contracts, leases with option to purchase, and any contract under which possession of the property is given to the purchaser but title is retained by the vendor as security for the payment of the purchase price. It also includes the furnishing of food, drink, or meals for compensation whether consumed upon the premises or not.

"Casual or isolated sale" means a sale made by a person who is not engaged in the business of selling the type of property involved. (Revised Code of Washington, Vol. 8, p. 3.)

82.04.060 *"Sale at wholesale," "wholesale sale."* "Sale at wholesale" or "wholesale sale" means any sale of tangible personal property which is not a sale at retail and means any charge made for labor and services rendered for persons who are not consumers, in respect to real or personal property, if such charge is expressly defined as a rental sale by RCW 82.04.050 when rendered to or for consumers: *Provided*, That the term "real or personal property" as used in this section shall not include any natural products named in RCW 82.04.100. (Revised Code of Washington, Vol. 8, pp. 5, 6.)

82.04.070 *"Gross proceeds of sales."* "Gross proceeds of sales" means the value proceeding or accruing from the sale of tangible personal property and/or for services rendered, without any deduction on account of the cost of property sold, the cost of materials used, labor costs, interest discount paid, delivery costs, taxes, or any other expense whatsoever paid or accrued and without any deduction on account of losses. (Revised Code of Washington, Vol. 8, p. 6.)

82.04.220 *Business and occupation tax imposed.* There is levied and shall be collected from every person a tax for the act or privilege of engaging in business activities. Such tax shall be measured by the application of rates against value of products, gross proceeds or sales, or gross income of the business, as the case may be. (Revised Code of Washington, Vol. 8, p. 9.)

82.04.270 *Tax on wholesalers, distributors.* (1) Upon every person except persons taxable under subsection (1) of RCW 82.04.260 engaging within this state in the business of making sales at wholesale; as to such persons the amount of tax with respect to such business shall be equal to the gross proceeds of sales of such business multiplied by the rate of one-quarter of one percent.

(2) The tax imposed by this section is levied and shall be collected from every person engaged in the business of distributing in this state articles of tangible personal property, owned by them from their own warehouse or other central location in this state to two or more of their own retail stores or outlets, where no change of title or ownership occurs, the intent hereof being to impose a tax equal to the wholesaler's tax upon persons performing functions essentially comparable to those of a wholesaler, but not actually making sales: *Provided,* That the tax designated in this section may not be assessed twice to the same person for the same article. The amount of the tax as to such persons shall be computed by multiplying one-quarter of one percent the value of the article so distributed as of the time of such distribution: *Provided,* That persons engaged in the activities described in this subsection shall not be liable for the tax imposed if by proper invoice it can be shown that they have purchased such property from a wholesaler who has paid a business and occupation tax to the state upon the same articles. This proviso shall not apply to purchases from manufacturers as defined in RCW 82.04.110. The tax commission shall prescribe uniform and equitable rules for the purpose of ascertaining such value, which value shall correspond as nearly as possible to the gross proceeds from sales at wholesale in this state of similar articles of like quality and character, and in similar quantities by other taxpayers: *Provided further,* That delivery trucks or vans will not under the purposes of this

section be considered to be retail stores or outlets. (Revised Code of Washington, Vol. 8, p.11.)

82.04.500 *Tax part of operating overhead.* It is not the intention of this chapter that the taxes herein levied upon persons engaging in business be construed as taxes upon the purchasers or customers, but that such taxes shall be levied upon, and collectible from, the person engaging in the business activities herein designated and that such taxes shall constitute a part of the operating overhead of such persons. (Revised Code of Washington, Vol. 8, p. 19.)

APPENDIX B

UNITED STATES CONSTITUTION

Art. I, Sec. 8, clause 3:

"The Congress shall have Power—

* * *

"To regulate Commerce * * * among the several States* * *"

Fourteenth Amendment, Sec. 1:

"* * * nor shall any State deprive any person of * * * property, without due process of law;* * *"